

## Michigan Jobs and Investment Act



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State Treasurer  
Michigan Department of Treasury  
House Tax Policy Committee  
April 13, 2005

## Tax Restructuring for the 21<sup>st</sup> Century

The Michigan Jobs and Investment Act will:

- Encourage businesses to invest and create jobs in Michigan
- Foster small business growth
- Attract the technology jobs of the future
- Provide broad based tax relief and promote business tax fairness
- Maintain fiscal integrity

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## Problems with Current System

- High personal property tax burden discourages investment in Michigan
- Apportionment formula discourages location in Michigan
- Overall burden very uneven across sectors
- Manufacturing burden too high
- SBT too insensitive to changes in profits
- SBT repealed effective 2010

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## Michigan Jobs and Investment Act

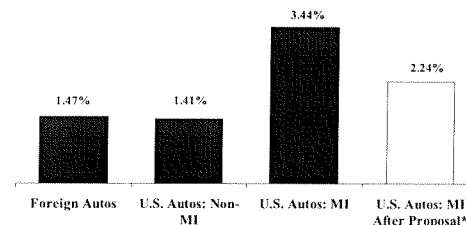
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## Creates & Retains Jobs

- Encourages investment through **35% personal property tax credit** for manufacturing and R&D
- Removes incentives to create jobs outside Michigan by adopting **100 percent sales factor**
- Fosters emerging technologies and the new economy by providing **R&D credits**
- Balances business taxes by having **less reliance on taxing labor** and more on taxing profits by adding into SBT base additional 2 times profits

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## Blended Property Tax Rates on M&E for the Automotive Industry



Michigan's property tax rates are 238% of the blended rate that U.S. and foreign autos pay in other states. This creates a disadvantage for Michigan based companies and is a significant hurdle that Michigan has to overcome to attract new capital investment.

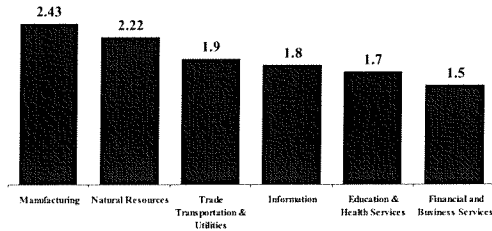
Tax rates on M&E are derived from the Minnesota Center for Public Research, 50 State Property Tax Comparison using an average of the largest city and a typical rural area in each state.

The TRRs are weighted based on 2003 production units for all U.S. assembly plants.

\*Based on a 35% PPT Credit

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## Manufacturing Has Highest Economic Multiplier



Note: Multiplier shows how much intermediate and final output is generated by a dollar's worth of final demand for industry's product

Source: NAM Council of Manufacturing Associations quoting BEA statistics

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## Apportionment Change Encourages Investment in Michigan

### Company A - Before Investment

	Michigan	Total
Sales	\$5,000,000	\$100,000,000
Payroll	\$1,000,000	\$10,000,000
Property	\$1,000,000	\$10,000,000
Apportionment Factor (at 90, 5, 5)		5.5%
Apportionment Factor (at 100, 0, 0)		5.0%

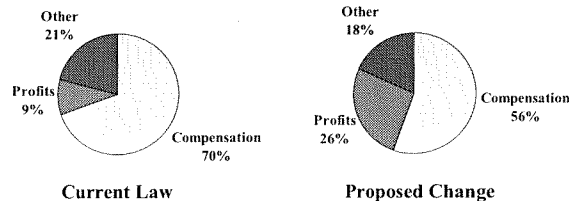
### Company A - After Investing in Michigan

	Michigan	Total
Sales	\$5,000,000	\$100,000,000
Payroll	\$2,000,000	\$11,000,000
Property	\$2,000,000	\$11,000,000
Apportionment Factor (at 90, 5, 5)		6.3%
Apportionment Factor (at 100, 0, 0)		5.0%

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## Plan Cuts Tax on Payroll

### Components of Tax Base



Note: Computed using tax return data for 1996-2001.

Source: Tax Analysis Division, Michigan Department of Treasury

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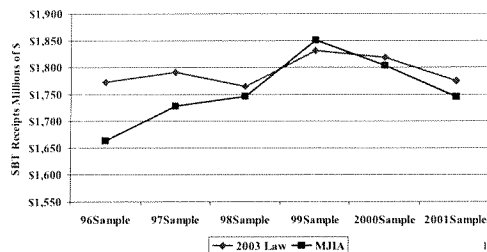
## Application of Profits Weighting

- Applies only to taxpayers filing as a corporation for federal purposes
- Does not apply to partnerships
- Does not apply to S-Corporations
- Does not apply to LLCs filing as partnerships

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## Outcome Similar Using Different Years

SBT Receipts (millions of \$)



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## Attracts Jobs of the Future

- Cuts the alternative rate for small businesses - from 2 percent to 1.2 percent
- Creates an R&D credit - Taxpayers would receive a credit for 1.2% of compensation paid to employees engaged in research and development

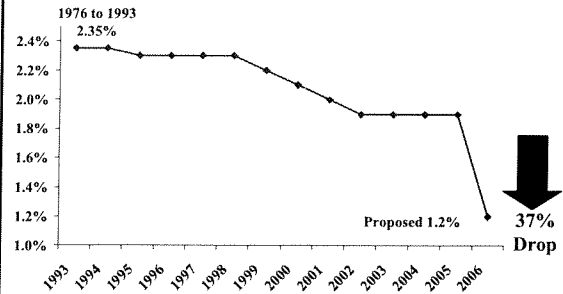
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## Provides Broad-Based Tax Relief

- Cuts standard SBT rate by 37%
- Cuts tax rate for small businesses by 40%
- 71,493 businesses will pay less
- 76 percent of businesses with a liability change pay less
- 67,440 taxpayers have no liability change
- 90,000 additional taxpayers are exempt from filing

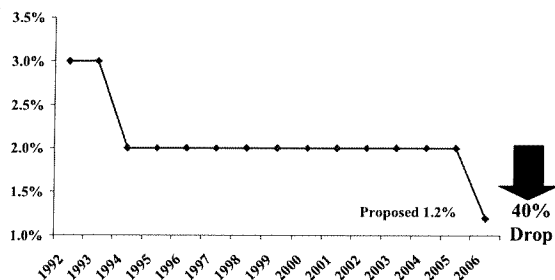
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## SBT Rate Falls 37 Percent



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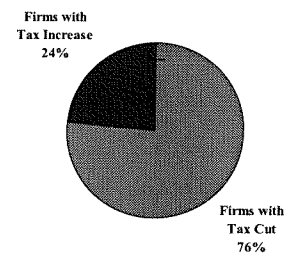
## Small Business Rate Cut 40 Percent



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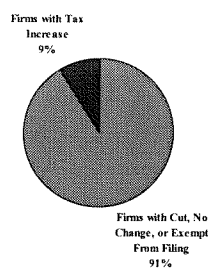
## Number of Firms Seeing Cut Triple Number with Increase

Statistics are for Firms with a Liability Change



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## 9 Out of 10 Firms See Tax Reduction or No Change



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## Simplifies Business Tax Structure

- Eliminates Excess Compensation Reduction
- Eliminates Gross Receipts Reduction
- Eliminates Special Credit for unincorporated businesses
- Eliminates special credit for telephone property taxes paid
- Makes small business credit eligibility independent of business organization or out of state affiliation
- Broadens the Base and Cuts the Rate

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## Fosters Business Tax Fairness

- 35% personal property tax credit mitigates differing tax burdens across sectors
- Changes the taxation of insurers to a 2 percent premiums tax like those imposed by most other states
- Eliminates special property tax treatment for commercial rental property - treats changes in value like all other value changes are treated for assessment purposes (WPW fix)

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## Who Pays Michigan SBT

### Size of Taxpayer 2001-02

Michigan Tax Base	# of Firms	Tax Liability	% Total
Over \$100,000,000	99	\$375,202,714	20.1%
\$10,000,000-\$99,999,999	1,689	\$548,768,173	29.4%
\$1,000,000-\$9,999,999	19,029	\$653,353,742	35.0%
\$100,000-\$999,999	78,941	\$259,104,158	13.9%
Less Than \$100,000	61,344	\$28,659,710	1.5%
Total	161,102	\$1,865,088,497	100.0%

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## Who Pays Michigan SBT

### Size of Liability 2001-02

Liability Class	# of Firms	Tax Liability	% Total
Greater than \$1,000,000	152	\$446,453,993	23.9%
\$100,001-\$1,000,000	2,571	\$613,690,300	32.9%
\$10,001-\$100,000	20,657	\$592,981,814	31.8%
\$1-\$10,000	80,775	\$211,962,390	11.4%
\$0	56,947	\$0	0.0%
Total	161,102	\$1,865,088,497	100.0%
Michigan Only Firms	133,219	\$792,915,210	42.5%
Multi-State Firms	27,883	\$1,072,173,287	57.5%

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## Who Pays Michigan SBT

### Sector Breakdown 2001-02

Sector	Liability	% of Total Liability
Transportation Equipment	\$83,146,993	4.5%
Other Manufacturing	\$399,700,054	21.4%
Services	\$483,779,255	25.9%
Retail Trade	\$285,190,084	15.3%
FIRE	\$129,988,352	7.0%
Other	\$483,283,759	25.9%
All Firms	\$1,865,088,497	100.0%

Note: Other category includes construction, wholesale trade, Agriculture, Mining, and Forestry.

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## Who Pays Michigan SBT

### Type of Firm Breakdown 2001-02

Type of Firm	# of Firms	% of Total Tax Liability	% Total
Individuals	15,904	\$31,128,014	1.7%
S Corporations	53,716	\$356,020,572	19.1%
Corporations	57,949	\$1,224,303,688	65.6%
Other *	33,533	\$253,636,223	13.6%
All Firms	161,102	\$1,865,088,497	100%

\*Includes fiduciary companies, professional corporations, partnerships, and limited liability companies.

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## Michigan Taxes At National Average

The Tax Foundation finds...

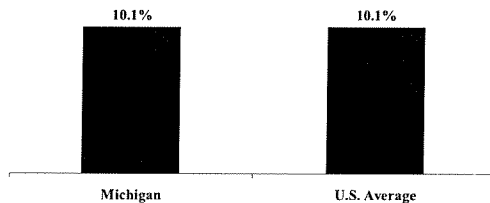
- Michigan ranks 22nd for state and local tax burden in 2005, down from 21st in 2004.
- Michigan's state and local tax burden as a percent of income is at national average of 10.1 percent.
- Michigan's state and local tax per capita tax burden of \$3,686 is below the national average of \$3,763.

Source: Tax Foundation, April 2005

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## Tax Foundation Finds Michigan Taxes At National Average for 2005

State and Local Taxes as a Percent of Income

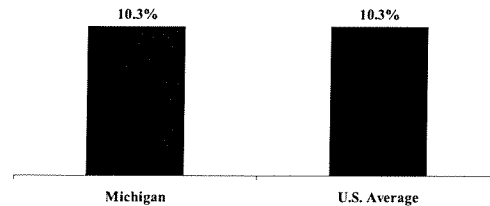


Source: Tax Foundation, April 2005

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## U.S. Census Data Show Michigan Taxes At National Average

FY 2002 State and Local Taxes as a Percent of Personal Income

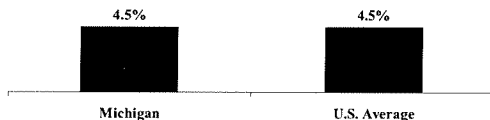


Source: Bureau of Economic Analysis; U.S. Census; Uses personal income from 6/04.

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## COST Study Puts Michigan Business Taxes at National Average

FY 2003 State and Local Business Taxes as a Percent of Personal Income

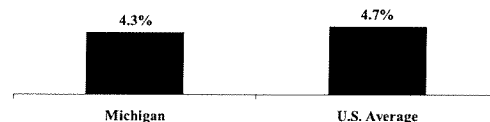


Source: Council on State Taxation, Bureau of Economic Analysis

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## Boston Fed Study Puts MI Business Taxes Below National Average

FY 2003 State and Local Business Taxes as a Percent of Personal Income

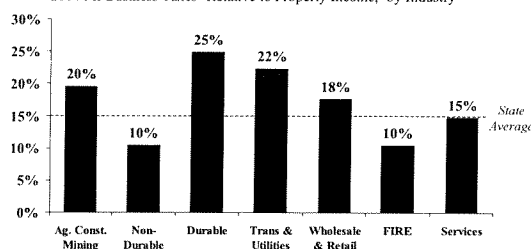


Source: Robert Tannenwald, Federal Reserve Bank of Boston

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## The Case for Business Tax Reform Disproportionate Taxes on Durable Manufacturing

2004 MI Business Taxes<sup>1</sup> Relative to Property Income,<sup>2</sup> by Industry



<sup>1</sup> Effective Tax Rates were calculated by dividing 2004 business taxes by average property income for the period 1999-2004.  
<sup>2</sup> "Property income" includes capital income plus the income of unincorporated businesses and rental income received by persons.  
<sup>3</sup> "Capital income" is the component of gross state product (GSP) that includes interest and distributed and undistributed corporate profits.

<sup>4</sup> Data derived from Ernst and Young calculations from April 2005.

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## Personal Property Tax

- 36 States including Michigan tax personal property
- Michigan exempts inventory (11 states tax)
- 15 states exempt manufacturing machinery and equipment (Michigan does not)
- Personal property 9.4 percent of property tax base
- Personal property taxes totaled \$1.59 billion in 2002

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## Personal Property Value by County

- The State's five largest counties account for 55.3% of total personal property taxable value
- There are 9 counties where personal property taxable value accounts for more than 15% of total county taxable value
- These 9 counties are small and account for less than 3 percent of total Michigan taxable value
- In 2004, there was 1 county where personal property accounted for more than 20 percent of its taxable value - this is down from 3 counties in 2002 and 5 counties in 2001

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## Taxation of Insurers

- Nearly all states impose a tax on insurance premiums.
- The median tax rate for the 50 states is 2% compared to Michigan's tax of 1.07 % before the application of several credits.
- Michigan's tax is the 4<sup>th</sup> lowest of the 50 states.
- 35 states have a premiums tax of 2% or higher.

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## Michigan Insurance Tax 4th Lowest in U. S.

1. Louisiana	\$2.90
2. Kentucky	\$2.81
3. Delaware	\$2.71
4. Nevada	\$2.56

U. S. Median	\$1.56
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**47. Michigan      \$0.76**

Tax per \$1,000 of personal income, FY 2003 State Tax Collections, U. S. Bureau of the Census

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## Insurance Companies Are Exempt From

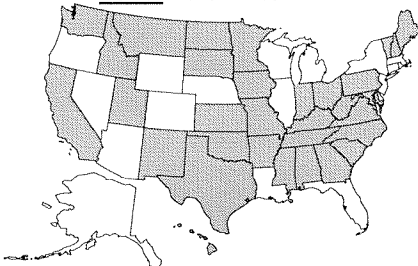
- Use tax on out-of-state purchases
- Use tax on telephone calls
- Use tax on leased equipment

**Other businesses pay these taxes!**

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## Higher Tax ≠ Higher Rates

**32 States with a Higher Premiums Tax have  
Lower Auto Rates than MI**



Sources: RIA Checkpoint, OFIS - State of Michigan, Insurance Information Institute

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## Insurance Tax Share of Corporate Taxes Still Low After MJIA

Insurance Taxes as a Percent of Total Corporate and Insurance Taxes

1. Washington	61.0%
2. Hawaii	58.6%
3. Nevada	46.5%
4. Wyoming	45.2%

U. S. Average	22.6%
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**38. Michigan (MJIA)      19.9%**

Insurance and total corporate taxes, FY 2003 State Tax Collections, U. S. Bureau of the Census

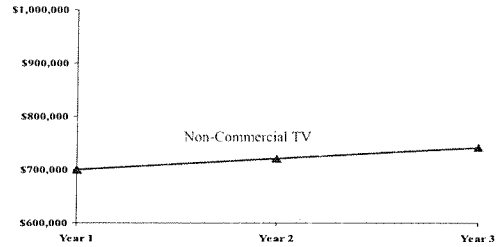
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## WPW

- Proposal A made changes to the definition of “additions” and “losses” for commercial property
- Additions include value increase attributable to increase in occupancy
- Losses include value decrease attributable to loss in occupancy
- WPW allows decreases in occupancy to lower property values, but caps additions based on taxable value cap

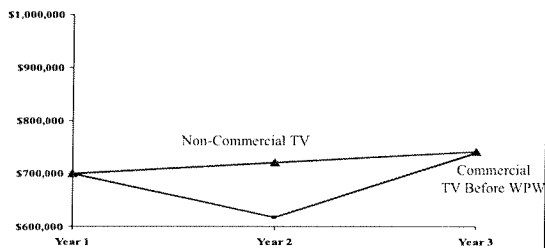
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## Changes in Taxable Value Before and After WPW Decision



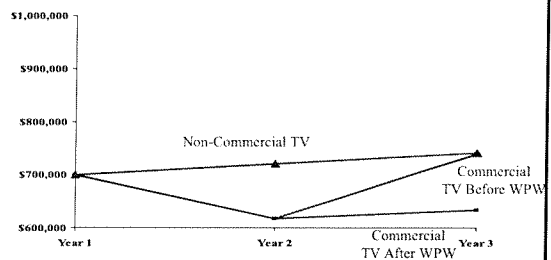
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## Changes in Taxable Value Before and After WPW Decision



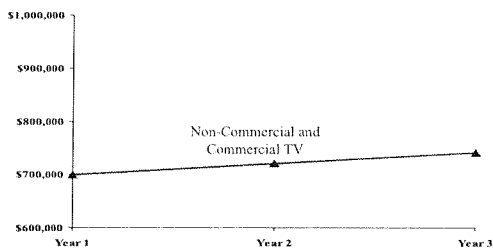
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## Changes in Taxable Value Before and After WPW Decision



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## Changes in Taxable Value After WPW Fix



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## Maintain Fiscal Integrity

- Prevents a 25% reduction in General Fund revenues in 2010
- Protects local government and school revenues
- Revenue neutral

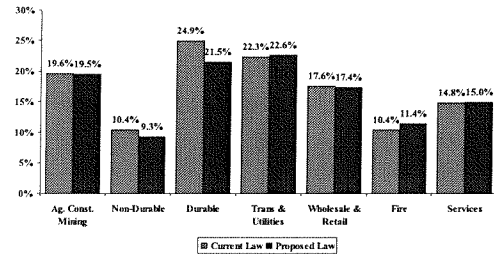
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## MJIA Components

	REVENUE (\$ millions)
Cut the Rate to 1.2 % for All SBT Taxpayers, including the alternative tax	(739)
Create a 35% Manufacturing Personal Property Tax Credit	(272)
Create a 35% R & D Personal Property Tax Credit	(15)
Create an R & D Compensation Credit	(20)
Change to 100% Sales Factor Apportionment	(40)
Adjustments to the Tax Base:	801
<ul style="list-style-type: none"> <li>Increase the weighting of profit in the SBT tax base</li> <li>Eliminate the excess compensation reduction</li> <li>Eliminate the gross receipts reduction</li> <li>Eliminate special credit for unincorporated businesses</li> <li>Eliminate special credit for telephone property taxes paid</li> <li>Treat compensation of employees leased from a professional employer organization as compensation of the client business</li> <li>Make small business credit eligibility independent of business organization or out of state affiliation</li> </ul>	
Change the Taxation of Insurers to a 2% Premiums Tax	255
Eliminate Special Property Tax Treatment for Commercial Rental Property.	30
<b>TOTAL</b>	<b>-6</b>

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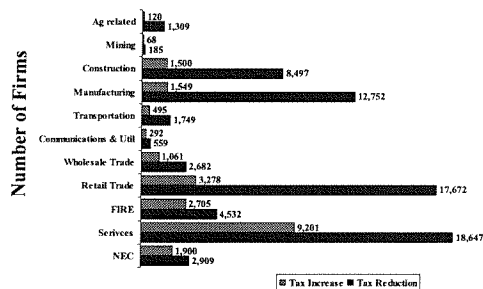
## Michigan Effective Total State and Local Tax Rates on Property Income



Note: Effective tax rates were calculated by dividing 2004 tax data by average property income for 2004. Data derived from Ernst and Young Calculations, April 2005.

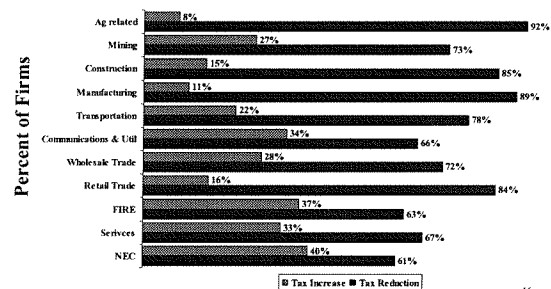
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## Three Times as Many Firms See a Tax Reduction



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## Three Times as Many Firms See a Tax Reduction



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## Who Gets a Tax Cut

Number	Type
32,293	Small Business Credit/Alternate Filers
8,654	Manufacturers Claiming Personal Property Credit
8,782	Straight Percentage Filers
16,566	Filers Claiming Excess Compensation Deduction
4,946	Filers Claiming Gross Receipts Deduction
252	Others
<b>71,493</b>	<b>Firms with a Tax Cut</b>

Firms listed in first relevant category

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## Tax Restructuring for the 21<sup>st</sup> Century

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